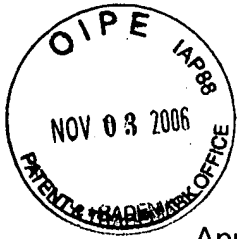


I hereby certify that this correspondence is being deposited with the United States Postal Service with sufficient postage as first class mail in an envelope addressed to: Mail Stop Amendment, Commissioner for Patents, P.O. Box 1450, Alexandria, VA 22313-1450 on October 31, 2006.



Alexandra Allison
Alexandra Allison PATENT

IN THE UNITED STATES PATENT AND TRADEMARK OFFICE

Applicant : Brent C. Abraham, et al.
Application No. : 09/866,544
Filed : May 25, 2001
Title : Apparatus, Systems and Methods for Transacting and Managing Like-Kind Exchanges
Grp./Div. : 3693
Examiner : Patel, Jagdish
Docket No. : PELK0002/MRK

Mail Stop Amendment
Commissioner for Patents
P.O. Box 1450
Alexandria, VA 22313-1450

140 S. Lake Ave., Suite 312
Pasadena, CA 91101-4710

**DECLARATION UNDER 37 C.F.R. SECTION 132
BY BRENT C. ABRAHM
FILED IN SUPPORT OF
AMENDMENT AND RESPONSE TO OFFICE ACTION DATED JULY 5, 2006**

1. I, Brent C. Abraham, am one of the inventors of the above-identified patent application. I am also one of the co-founders of eLKE.com, LLC, since renamed Accruit, LLC, the assignee of the above-identified patent application. Presently, I am Executive Vice President of Business Development for Accruit, LLC ("Accruit").

2. I have a B.A. degree in International Business and Marketing from University of Alabama.

3. Prior to founding eLKE.com, LLC, I had worked for many years, beginning in 1990 as a materials management analyst, for an internationally known, major oil company. During the early 1990's, not long after the federal government released "safe-harbor" regulations further supporting United States Internal

Revenue Code Section 1031 (the "Like-Kind Exchange Statute"), originally enacted in 1921, I participated in a corporate-wide initiative to re-engineer the company's business processes for acquisition, utilization, management and disposition of assets. As a result of that corporate-wide initiative, I participated in, and helped staff, a new department dedicated to asset management for the corporation. As part of the mission of that new asset management department, I spearheaded an initiative for identifying and transacting like-kind exchanges for various assets. Notwithstanding the immense resources available through that corporation, the asset management department's processes were manually based.

4. At the time that I co-founded the unincorporated predecessor of eLKE.com, LLC in 1999, it is my belief and understanding that large-scale, like-kind exchanges were being handled, using primarily manual procedures, by "brick-and-mortar" qualified intermediaries.

5. It is my belief and understanding that, in 1999 and earlier, the average value of single exchanges was approximately \$250,000. It is my belief and understanding, and it was that belief and understanding on which the entire business plan for eLKE.com, LLC was based, that until that time, even though smaller-scale (i.e., for values less than \$250,000) exchanges were theoretically possible under the Like-Kind Exchange Statute (United States Internal Revenue Code Section 1031), and even though there was a huge untapped volume of such smaller-scale exchanges, such smaller-scale, like-kind exchanges were not economically feasible. Further, it is my belief and understanding that, in 1999 and earlier, except for large-scale transactions, small businesses did not typically endeavor to participate in the potential for tax-deferred benefits of Section 1031 exchanges.

6. It is my belief and understanding that a main reason that such smaller-scale like-kind exchanges had not been economically feasible was due in great part to the complexity of the requirements for complying with the details of the Section 1031 statute. It is my belief and understanding that although large corporations might employ tax and business professionals in house that would be knowledgeable enough to structure like-kind exchanges in compliance with the Like-Kind Exchange Statute, small businesses typically hired outside counsel to structure such exchanges. Further, it is my belief and understanding that, in 1999 and earlier, "brick-and-mortar" qualified intermediaries charged a percentage of the value of the exchange transaction, or in some cases, a standard fee plus a percentage of the interest recorded on the funds for an exchange in escrow, as a commission for transacting the exchange. Because the detailed requirements of the Section 1031 statute were complex, it is my belief and understanding that "brick-and-mortar" qualified intermediaries did not find the standard percentage commission for smaller-scale, like-kind exchanges to be cost-justified. Further, it is my belief and understanding that in 1999 and earlier, taxpayers did not find the standard fees charged by qualified intermediaries, plus the fees by tax advisors and attorneys, to conduct smaller-scale, like-kind exchanges to be economically feasible.

7. In order for a taxpayer to qualify for the "safe harbor" requirement contained in Treas. Reg. section 1.1031(k)-1(g)(5) and (h) of the Like-Kind Exchange Statute, it is my belief and understanding that a primary function of a "brick-and-mortar" qualified intermediary was to act as an assignee of rights regarding the receipt of funds for an asset sold, and to receive such funds, and to disburse funds for the purchase of a replacement property, and to receive title for that replacement property, and to subsequently convey title to that replacement property to the taxpayer. It is my belief and understanding that the aforementioned functions of a "brick-and-mortar" qualified intermediary were provided so that, in order to qualify for the "safe harbor" requirement contained in

Treas. Reg. section 1.1031(k)-1(g)(5) and (h) of the Like-Kind Exchange Statute, a like-kind-exchange taxpayer would not be considered to be in actual or constructive receipt of funds or other property until the taxpayer received the like-kind replacement property.

8. Because of the complexity and intricacies of the Like-Kind Exchange Statute, it is my belief and understanding that in 1999 and earlier, large corporations, such as the major international oil company for which I had worked, typically employed tax and business professionals who could manually structure a relatively "simple" like-kind exchange so that the exchange would have a strong chance of qualifying for tax-deferred treatment. It is my belief and understanding that, typically, such "simple" exchanges were structured to exchange identical types of assets so that the exchange would meet the requirements of the Like-Kind Exchange Statute. For example, an exchange of real estate for replacement real estate could be structured and scheduled so that the exchange would meet the requirements of the Like-Kind Exchange Statute. Or, as another example, an exchange of a used oil rig for a new oil rig might be structured. However, the Like-Kind Exchange Statute does not require identical asset type exchanges in order for an exchange to qualify for tax-deferred treatment. Rather, in order for an exchange to be considered an exchange of like-kind assets, the safe harbor provisions of the Like-Kind Exchange Statute allow that exchanged assets must be in the same General Asset Class or Product Class. See, e.g., Specification of the Present Application ("Specification"), p. 27, lines 1-5 ("If Taxpayer exchanges relinquished property for replacement property listed in the same Rev. Proc. 87-56 General Asset Class or SIC Product Class, that exchange will be considered as an exchange of like-kind property, even though the applicable General Asset Class or Product Class is not specifically enumerated in the Treas. Reg. section 1.1031(a)-2(b)(2) or (3) "like-class" safe harbor."). Even so, because of the intricacies of ensuring compliance with the Like-Kind Exchange Statute, it is my belief and recollection that, in 1999 and

earlier, identical-type "simple" exchanges were the most typical types of exchanges structured.

9. Further, it is my belief and recollection that, because of the complexity and intricacies of the requirements of the Like-Kind Exchange Statute, smaller-scale, like-kind exchange transactions and/or exchanges of non-identical asset types were not typically structured in 1999 and earlier.

10. Recognizing what we believed to be a huge untapped volume of smaller-scale and/or non-identical asset type exchanges, Todd Fisher, the other inventor named in the present application, and I set about inventing and developing an Internet-based, online qualified-intermediary system that could be used by taxpayers for smaller-scale, and/or non-identical asset type exchanges, as well as for large-scale, and/or identical asset type like-kind exchanges.

11. It is my belief and understanding that a qualified intermediary would be disqualified as a qualified intermediary, under the Like-Kind Exchange Statute, if the qualified intermediary acted, for example, as the taxpayer's agent or attorney. See, e.g., Specification, p. 38, lines 9-18 ("A qualified Intermediary is defined in Treas. Reg. section 1.1031(k)-1(g)(4)(iii) as a person who: (1) is not the taxpayer or a disqualified person; and (2) enters into a written exchange agreement with the taxpayer and, as required by the exchange agreement, acquires the relinquished property from the taxpayer, transfers the relinquished property, acquires the replacement property, and transfers the replacement property to the taxpayer. According to Treas. Reg. section 1.1031(k)-1(k)(2), the term "disqualified person" includes a person who is the taxpayer's agent at the time of the transaction. For this purpose, a person who has acted as the taxpayer's employee, attorney, accountant, investment banker or broker or real estate agent or broker within the two-year period ending on the date of the transfer of the first of the relinquished properties is treated as the taxpayer's agent.").

Notwithstanding the disqualification provisions by the Like-Kind Exchange Statute, it is my belief and understanding that testing the parameters of a proposed like-kind exchange against the published safe-harbor provisions does not constitute a disqualifying act. See, e.g., Specification, p. 38, lines 19-27 (“... performance of certain services does not cause an entity to be a “disqualified person.” These services include: (1) services for the taxpayer with respect to exchanges of property intended to qualify for nonrecognition of gain or loss under section 1031; and (2) routine financial, title insurance, escrow or trust services for the taxpayer by a financial institution, title insurance company, or escrow company.”).

12. In 2002, the Internal Revenue Service issued a Private Letter Ruling approving deferred, multi-property, like-kind exchanges using an online qualified intermediary that operates electronically through an Internet site. Attached hereto as Exhibit A, is a true and correct printout of Private Letter Rules Number 200236026, dated September 6, 2002 (the “Private Letter Ruling”, or the “PLR”). Also attached hereto, as Exhibit B, is a true and correct printout of a Federal Taxes Weekly Alert by RIA (the “RIA Alert”), dated September 19, 2002, Volume 48, No. 39, presenting commentary regarding the IRS Private Letter Ruling (“PLR 200236026”) regarding like-kind exchanges using what the RIA Alert terms to be a “virtual” qualified intermediary (“... namely one that operates electronically through an Internet site.” RIA Alert, p. 1, ¶1). The RIA Alert states that “[t]he favorable new ruling makes it easier for sellers to legitimately avoid paying tax on the sale of a non-inventory asset if they tend to reinvest the sales proceeds in like-kind property.” Ex. B, RIA Alert, “PLR 200236026,” p. 1, ¶2.

13. As a result of implementing our Internet-based, online qualified-intermediary system, it is my belief, opinion and understanding that Accruit, LLC will process approximately 150,000 like-kind exchange transactions (sales and purchase transactions) during 2006, including smaller-scale, like-kind exchanges

valued, on average, \$35,000, and including exchanges of individual assets valued as low as \$4.

14. It is my opinion, belief and understanding that the smaller-scale, like-kind exchanges transacted through Accruit's Internet-based, online qualified-intermediary system are due in part to the novel ability of Accruit's Internet-based, online qualified-intermediary system to substantially simultaneously test various features of a proposed like-kind exchange transaction up-front to determine if the features of the proposed like-kind exchange transaction collectively meet Section 1031 "safe-harbor" provisions.

15. Further, it is my opinion, belief and understanding that many small business entities, which can not necessarily afford to employ specialized tax and accounting professionals to structure a like-kind exchange, now use Accruit's Internet-based, online qualified-intermediary system to test proposed like-kind exchanges and manage like-like exchange transactions. It is my opinion, belief and understanding that small business entities use Accruit's Internet-based, online qualified-intermediary system because, among other reasons, it both pre-tests proposed like-kind exchange transactions against the safe-harbor provisions of the Like-Kind Exchange Statute, and facilitates exchange transactions that comply with those safe-harbor provisions. See, e.g., Ex. A, Private Letter Ruling.

16. I hereby declare that all statements made herein of my own knowledge are true and that all statements made on information and belief are believed to be true; and further that the statements were made with the knowledge that willful false statements and the like so made are punishable by fine or imprisonment, or

Application No. 09/866,544

Declaration Under Section 132 by Brent C. Abrahm

both, under Section 1001, Title 18 of United States Code and that such willful false statements may jeopardize the validity of the application or any corresponding U.S. patent.

Date:

October 30, 2006



Brent C. Abrahm

Internal Revenue Service



Number: **200236026**
Release Date: 9/6/2002
Index No.: 1031.05-00

Department of the Treasury

Washington, DC 20224

Person to Contact:

Telephone Number:

Refer Reply To:

CC:ITA:4 – PLR-118622-01

Date:

June 3, 2002

In Re:

LEGEND:

A =

B =

C =

m =

x =

QI =

Date 1 =

Date 2 =

Date 3 =

Date 4 =

Date 5 =

Dear

This letter responds to your request for a private letter ruling, dated February 26, 2001, submitted on behalf of A, concerning § 1031 of the Internal Revenue Code. Additional information was submitted in letters dated August 28, 2001, and May 29, 2002.

FACTS

A, a wholly owned subsidiary of B, is engaged in the business of m. A, a calendar year taxpayer, files a consolidated income tax return as part of an affiliated group of corporations. All of the corporations in the affiliated group use the accrual method of accounting.

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A's business requires it to periodically dispose of certain properties and/or equipment, some of which is co-owned by other parties, and reinvest in like-kind property. A seeks to characterize the transactions as non-taxable exchanges under § 1031.

QI has developed a World Wide Web site that facilitates online like-kind exchanges by using the Internet and electronic or wire funds transfers to accomplish these exchanges. QI is an independent third party whose only relationship with A is in connection with the performance of services for A's transactions intended to qualify under § 1031.

Each authorized user with the right to access QI's secured site has a unique user name and password to access the system. For agreements signed on-line by a particular user, the user confirms that he or she wants to sign the agreement before the document is processed by the on-line system. For any documents that a representative of the QI is required to sign, an electronic agent is utilized to sign that document with the appropriate signature. The system then stores a complete copy of the document with the name of each signer and the time and date that each person signed it. The document is provided a digital thumbprint that generates a unique code for each signature associated with a document. The document cannot be altered without modifying the digital thumbprint. A represents that online methods of executing agreements, transmitting notices of assignments, and making replacement property identifications satisfy the requirements of the Electronic Signatures in Global and National Commerce Act, Pub. L. No. 106-229, 114 Stat. 464 (2000) (the Act).¹

A and QI entered into an agreement on Date 1 pursuant to which QI agreed to serve as the qualified intermediary for certain transactions, including those addressed in this letter ruling. A, by executing an agreement with QI, may use QI's website to access its process for engaging in deferred multiple-batch, like-kind exchanges. Upon execution of the agreement, QI opened a segregated account for its transactions with A. Each multiple-batch transaction has its own unique subaccount within QI's records. The agreement (1) restricts the use of the proceeds from the sale of relinquished property to the purchase of like-kind replacement property, (2) restricts the payment to A of the sale proceeds and any interest credited to A on those proceeds, and (3) assigns to QI A's rights to sell relinquished property under sale agreements and rights to purchase replacement property under purchase agreements.

The agreement prescribes a "sale period" for each batch account of A, during which one or more items of relinquished property may be transferred by A, with the proceeds from the sale of that relinquished property being received by QI's bank and credited to A's applicable batch account. After the sale period expires, the proceeds in that batch account are reinvested by QI in like-kind replacement property in accordance with A's

¹In general, the Act provides that a signature, contract or other record relating to a transaction may not be denied legal effect, validity, or enforceability solely because it is in electronic form. § 101(a). However, the Act does not limit or supersede any requirement by a Federal regulatory agency that records be filed with such agency in accordance with specified standards or formats. § 104(a).

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instructions. A purchases production equipment and materials from numerous vendors. Only equipment and materials that fall within C are included in the like-kind exchange process. A completes an online questionnaire to enable QI to send the wiring instructions and notice of assignment of rights to each purchaser.

QI's bank will receive and deposit the proceeds from the sale of the relinquished property into QI's bank account. A, through QI's website, will then direct QI to reinvest the restricted proceeds from the sale of the relinquished property in like-kind replacement property.

Exchange 1

On Date 2, A agreed to sell to purchaser 1 equipment used in A's trade or business on a property x% owned by A. Purchaser 1 was notified of A's assignment of rights to QI under A's agreement with QI. The agreement provided that title to the property passed from A to purchaser 1 on Date 3, the date purchaser 1 paid for the property in full. After A and purchaser 1 agreed to the terms and conditions of the sale, A completed the online questionnaire on QI's website to inform QI of the sale. Upon receiving notification, QI directed purchaser 1 to send the proceeds directly to QI. Only the funds that QI deposited into the net proceeds account were available to be reinvested in like-kind property. In accordance with the agreement executed by A and QI, A has no rights to receive, pledge, borrow, or otherwise obtain the benefits of money or other property held in the net proceeds account maintained by QI.

A located and agreed to acquire like-kind replacement property. Prior to acquisition of the replacement property, the seller of the replacement property was notified of A's assignment of rights to QI to purchase replacement property. A acquired the replacement property before the expiration of both the identification period and the exchange period set forth in § 1031(a)(3) and § 1.1031(k)-1(b).

Exchange 2

On Date 4, A agreed to sell and purchaser 2 agreed to buy equipment used in A's trade or business on a property that A owned in its entirety. Purchaser 2 was notified of A's assignment of rights to QI under A's agreement with QI. QI instructed purchaser 2 to send the sale proceeds directly to QI. On Date 5, purchaser 2 tendered full payment of the sale proceeds to QI. Only the funds that QI deposited into the net proceeds account were available to be reinvested in like-kind property. In accordance with the agreement executed by A and QI, A has no rights to receive, pledge, borrow, or otherwise obtain the benefits of money or other property held in the net proceeds account maintained by QI.

A located and agreed to acquire like-kind replacement property. Prior to acquisition of the replacement property, the seller of the replacement property was notified of A's assignment of rights to QI to purchase replacement property. A acquired the replacement property before the expiration of both the identification period and the exchange period set forth in § 1031(a)(3) and § 1.1031(k)-1(b).

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For both Exchange 1 and Exchange 2 it is represented that both the buyer of the relinquished property and the seller of the replacement property were notified of the assignment of A's rights regarding the transaction. The buyers were notified through e-mails that contained wiring instructions and the notification of assignment of rights. The purchaser was notified via a blanket notification, which the purchaser signed and returned to A. Further, A is able to provide a specific description of the property being divested as well as the replacement property being acquired. It is represented that the equipment involved in the exchanges is identified by model number and serial number.

LAW AND ANALYSIS

Section 1031(a)(1) of the Code provides that no gain or loss shall be recognized on the exchange of property held for productive use in a trade or business or for investment if such property is exchanged solely for property of like kind which is to be held either for productive use in a trade or business or for investment. Section 1031(a)(2) adds that this subsection does not apply to any exchange of stock in trade or other property held primarily for sale.

There are three general requirements for nonrecognition treatment under § 1031: (1) both the property surrendered and the property received must be held either for productive use in a trade or business or for investment; (2) the property surrendered and the property received must be of "like-kind;" and (3) there must be an exchange as distinguished from a sale and a purchase.

HELD FOR REQUIREMENT

The property owned by A and exchanged in the above-described transactions is equipment used by A in the business of m. Similarly, the property received by A will be used in that same business. Thus, the relinquished equipment that A disposes of and the replacement equipment that A acquires is considered property held for productive use in A's trade or business.

LIKE-KIND REQUIREMENT

The requirement that the exchanged properties be of like kind refers to the nature or character of the property and not to its grade or quality. Section 1.1031(a)-1(b). To qualify for like-kind exchange treatment, one kind or class of property may not be exchanged for property of a different kind or class. Under § 1.1031(a)-2(b), depreciable tangible personal property is of a like class to other depreciable tangible personal property if the exchanged properties are either within the same General Asset Class or within the same Product Class. It is represented that all of the personal property involved in the subject exchanges falls within the same product class.

When an exchange transaction is deferred, rather than simultaneous, even if the taxpayer trades property for like-kind property, the exchanged properties will not be of like kind if the replacement property is not timely identified and timely received. Section 1031(a)(3) and § 1.1031(k)-1(b) state that any property received by the taxpayer shall be treated as property that is not like-kind property if (a) such property is not identified

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as property to be received in the exchange on or before the day that is 45 days after the date on which the taxpayer transfers the property relinquished in the exchange, or (b) such property is received after the earlier of (i) the day that is 180 days after the date on which the taxpayer transfers the property relinquished in the exchange or (ii) the due date (determined with regard to extension) for the transferor's return of the tax imposed by this chapter for the taxable year in which the transfer of the relinquished property occurs. In the present case, the requirements of § 1031(a)(3) and § 1.1031(k)-1(b) are satisfied because the acquisitions of replacement property occurred prior to the expiration of both the identification period and the exchange period.

EXCHANGE REQUIREMENT

For purposes of §§ 1031 and 1.1031(k)-1, a deferred exchange is defined as an exchange in which, pursuant to an agreement, the taxpayer transfers property held for productive use in a trade or business or for investment (the "relinquished property") and subsequently receives property to be held either for productive use in a trade or business or for investment (the "replacement property"). In order to constitute a deferred exchange, the transaction must be an exchange (*i.e.*, a transfer of property for property, as distinguished from a transfer of property for money). Section 1.1031(k)-1(a). In the case of a transfer of relinquished property in a deferred exchange, gain or loss may be recognized if the taxpayer actually or constructively receives money or property which does not meet the requirements of § 1031(a) before the taxpayer actually receives like-kind replacement property. If the taxpayer actually or constructively receives money or property that does not meet the requirements of § 1031(a) in the full amount of the consideration for the relinquished property, the transaction will constitute a sale, and not a deferred exchange, even though the taxpayer may ultimately receive like-kind replacement property. According to § 1.1031(k)-1(f)(2), actual or constructive receipt of money or other property by an agent of the taxpayer (determined without regard to paragraph (k) of this section) is actual or constructive receipt by the taxpayer.

Section 1.1031(k)-1(g) of the regulations sets forth four safe harbors, the use of any of which will result in a determination that the taxpayer is not in actual or constructive receipt of money or other property for § 1031 purposes. Section 1.1031(k)-1(g)(4)(i) of the regulations provides that, in the case of a taxpayer's transfer of relinquished property involving a qualified intermediary, the qualified intermediary is not considered the taxpayer's agent for § 1031 purposes. In such a case, the taxpayer's transfer of relinquished property and subsequent receipt of like-kind replacement property is treated as an exchange, and the determination of whether the taxpayer is in actual or constructive receipt of money or other property before the taxpayer actually receives like-kind replacement property is made as if the qualified intermediary is not the agent of the taxpayer. Section 1.1031(k)-1(g)(4)(ii) provides that § 1.1031(k)-1(g)(4)(i) applies only if the agreement between the taxpayer and the qualified intermediary expressly limits the taxpayer's right to receive, pledge, borrow, or otherwise obtain the benefits of money or other property held by the qualified intermediary as provided in § 1.1031(k)-1(g)(6).

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A qualified intermediary, as defined in § 1.1031(k)-1(g)(4)(iii)(A), must be a person who is not the taxpayer or a disqualified person. According to § 1.1031(k)-1(k)(2) of the regulations, the term "disqualified person" includes a person who is the taxpayer's agent at the time of the transaction. For this purpose, a person who has acted as the taxpayer's employee, attorney, accountant, investment banker or broker, or real estate agent or broker within the two-year period ending on the date of the transfer of the first of the relinquished properties is treated as the taxpayer's agent at the time of the transaction. However, performance of certain services does not cause an entity to be a "disqualified person." These services include (a) services for the taxpayer with respect to exchanges of property intended to qualify for nonrecognition of gain or loss under § 1031, and (b) routine financial title insurance, escrow, or trust services for the taxpayer by a financial institution, title insurance company, or escrow company.

A qualified intermediary is a person who enters into a written agreement with the taxpayer (the "exchange agreement") and, as required by the exchange agreement, acquires the relinquished property from the taxpayer, transfers the relinquished property, acquires the replacement property, and transfers the replacement property to the taxpayer. Section 1.1031(k)-1(g)(4)(iii)(B). Regardless of whether an intermediary acquires and transfers property under general tax principles, an intermediary is treated as acquiring and transferring the relinquished property if the intermediary (either on its own behalf or as the agent of any party to the transaction) enters into an agreement with a person other than the taxpayer for the transfer of the relinquished property to that person, and pursuant to that agreement, the relinquished property is transferred to that person. Section 1.1031(k)-1(g)(4)(iv)(B). An intermediary is treated as acquiring and transferring replacement property if the intermediary (either on its own behalf or as the agent of any party to the transaction) enters into an agreement with the owner of the replacement property for the transfer of that property and, pursuant to that agreement, the replacement property is transferred to the taxpayer. Section 1.1031(k)-1(g)(4)(iv)(C). For these purposes, an intermediary is treated as entering into an agreement if the rights of a party to the agreement are assigned to the intermediary and all parties to that agreement are notified in writing of the assignment on or before the date of the relevant transfer of property. Section 1.1031(k)-1(g)(4)(v).

In the present case, purchaser 1 and purchaser 2 tendered full payment of the proceeds of the sale of the relinquished property to QI. Further, in accordance with the agreement executed by A and QI, A has no rights to receive, pledge, borrow, or otherwise obtain the benefits of money or other property held in the account, maintained by QI, in which the money was credited as required by §§ 1.1031(k)-1(g)(4)(ii) and (6)(i) of the regulations. Thus, A is not in actual or constructive receipt of proceeds of relinquished property.

QI is an independent third party that has not previously performed services for A. As such, QI will not be a "disqualified person" under § 1.1031(k)-1(k). Further, A assigned to QI its rights to sell relinquished property. In the case of both Exchange 1 and Exchange 2, the purchaser received notice of the assignment before the time that the relinquished property was transferred to the purchaser. Thus, QI will be treated as acquiring and transferring the relinquished property pursuant to §§ 1.1031(k)-1(g)(4)(iv)(B) and (v).

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Lastly, A assigned its right to purchase replacement property to QI. The sellers in the transactions described above received notice of the assignment before the time that the replacement property is transferred to A. Thus, QI will be treated as acquiring and transferring the replacement property pursuant to § 1.1031(k)-1(g)(4)(iv)(C) and (v). Accordingly, QI, acting in accordance with the agreement, will be treated as a qualified intermediary as defined in § 1.1031(k)-1(g)(4)(iii) of the regulations and will be treated as acquiring and transferring the relinquished property and the replacement property for purposes of § 1031.

BASIS OF REPLACEMENT PROPERTY

Section 1031(d) provides that if property was acquired in an exchange described in § 1031, then the basis shall be the same as that of the property exchanged, decreased in the amount of any money received by the taxpayer, and increased in the amount of gain or decreased in the amount of loss to the taxpayer recognized on such exchange. If the property so acquired consisted in part of the type of property permitted by § 1031 to be received without the recognition of gain or loss, and in part of other property, the basis shall be allocated between the properties (other than money) received, and for the purpose of the allocation, there shall be assigned to such other property an amount equivalent to its fair market value at the date of the exchange.

Based on the facts and representations you provided, and the above analysis, we rule as follows:

For purposes of determining whether Exchange 1 and Exchange 2 qualify for non-recognition of gain or loss under § 1031--

- (1) A's transfer of each batch of relinquished properties, and the corresponding receipt of related replacement properties, will be treated as a separate and distinct like-kind exchange for purposes of the nonrecognition provisions of § 1031.
- (2) QI, acting in accordance with the agreement between QI and A, will be treated as a qualified intermediary as defined in § 1.1031(k)-1(g)(4)(iii) of the regulations for purposes of the relinquished property and replacement property under § 1031.
- (3) Pursuant to §§ 1.1031(k)-1(f) and (g) of the regulations, A will not be in constructive receipt of any of the proceeds from the sale of relinquished property or any money or other property held by QI unless and until such amounts or items are actually received by A (*i.e.*, if replacement property is not acquired during the exchange period and the related sale proceeds are transferred to A).
- (4) Any interest received by A will comply with the safe harbor requirement of § 1.1031(k)-1(g)(5) and (h) and, therefore, will not result in A's being in actual or constructive receipt of money or other property before A actually receives like-kind replacement property. However, the interest is includible in income under

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§61 and cannot be deferred under §1031, even if it is reinvested in like-kind replacement property.

- (5) The basis of the replacement property received by A will be the aggregate adjusted bases of the relinquished properties in the exchange, decreased by any money received by A in the exchange and increased by the amount of any gain or decreased by any loss recognized by A in the exchange, allocated among the replacement properties received in proportion to their relative fair market values.

A copy of this letter must be attached to any income tax return to which it is relevant. We enclose a copy of the letter for this purpose. Also enclosed is a copy of the letter ruling showing the deletions proposed to be made in the letter when it is disclosed under § 6110 of the Internal Revenue Code.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any item discussed or referenced in this letter. This ruling is directed only to the taxpayer(s) requesting it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

Sincerely,
Stephen Toomey
Assistant to the Branch Chief
Office of Associate Chief Counsel
(Income Tax & Accounting)


Enclosures (2)

cc:

IRS OKs deferred multi-property like-kind exchanges through "virtual" qualified intermediary

PLR 200236026

In a private letter ruling, IRS approved deferred multi-property exchanges using a "virtual" qualified intermediary, namely one that operates electronically through an Internet site.

 **PRIA observation:** The favorable new ruling makes it easier for sellers to legitimately avoid paying tax on the sale of a non-inventory asset if they intend to reinvest the sales proceeds in like-kind property.

Background. Under Code Sec. 1031, gain or loss isn't recognized currently on the exchange of property held for productive use in a trade or business or for investment for property of like kind that will be held for productive use in a trade or business or for investment. The replacement property must be identified within 45 days after the date that the property given up is relinquished, and received no later than (a) 180 days after the date that the property given up is relinquished, or (b) the unextended due date for the taxpayer's return for the year in which the relinquished property is given up, whichever is earlier. (Code Sec. 1031(a)(3))

When a two-way (or direct) exchange of like-kind property isn't possible, the solution often is a multiparty deferred exchange. Seller can use the services of a qualified intermediary (QI) under Reg. § 1.1031(k)-1(g)(4). The QI acquires the relinquished property from Seller, transfers the relinquished property to a buyer, acquires suitable replacement property designated by Seller, and then transfers the replacement property to Seller. The determination of whether Seller is in actual or constructive receipt of money or other property before he actually receives like-kind replacement property is made as if the QI is not Seller's agent. This applies only if the agreement between Seller and QI expressly limits Seller's right to receive, pledge, borrow, or otherwise obtain the benefits of money or other property held by the QI. (Reg. § 1.1031(k)-1(g)(4)(ii))

An intermediary is treated as acquiring and transferring relinquished and replacement properties if it (either on its own behalf or as the agent of any party to the transaction) enters into an agreement with:

- ... a person other than Seller for the transfer of the relinquished property to that person, and under that agreement, the relinquished property is transferred to that person; and (Reg. § 1.1031(k)-1(g)(4)(iv)(B))
- ... the owner of the replacement property for the transfer of that property and, under that agreement, the replacement property is transferred to Seller. (Reg. § 1.1031(k)-1(g)(4)(iv)(C))

An intermediary is treated as entering into an agreement if the rights of a party to the agreement are assigned to the intermediary and all parties to that agreement are notified in writing of the assignment on or before the date of the relevant transfer of property. (Reg. § 1.1031 (k)-I (g)(4)(v))

Thoroughly modern swaps. The new ruling is addressed to a corporation we'll call ABC, which periodically sells equipment used in its business and buys replacement equipment, and QI, an independent third-party company that uses the Internet and electronic or wire funds transfers to facilitate on-line exchanges. QI's system uses unique user names and passwords for users. QI represents that its online methods of executing agreements, transmitting notices of assignments, and making replacement property identifications satisfy the requirements of the Electronic Signatures in Global and National Commerce Act (P.L. 106-229).

Under QI's agreement to act as ABC's qualified intermediary to help it complete deferred multiple-batch, like-kind exchanges, QI opens a segregated account for its transactions with ABC. Each multiple-batch transaction has its own unique subaccount within QI's records. The agreement:

- ... restricts the use of proceeds from the sale of relinquished property to the purchase of like-kind replacement property,
- ... restricts the payment to ABC of the sale proceeds and any interest credited to ABC on those proceeds, and
- ... assigns to QI all of ABC's rights to sell relinquished property under sale agreements and rights to purchase replacement property.

During a designated "sale period," proceeds from the sale of relinquished property are transferred to QI's bank and credited to ABC's applicable batch account. ABC, through QI's website, then directs QI to reinvest the restricted proceeds from the sale of the relinquished property in like-kind replacement property.


Electronic exchange. One of two exchanges described in the ruling is consummated as follows: ABC agrees to sell equipment used in its business to a buyer, who is notified of ABC's assignment of rights to QI, and is instructed by QI to send the sale proceeds directly to QI. Only the funds that QI deposited into the net proceeds account are available for reinvestment in like-kind property. ABC has no rights to receive, pledge, borrow, or otherwise obtain the benefits of money or other property held in the net proceeds account maintained by QI. ABC locates and agrees to buy like-kind replacement property, but before the acquisition, the seller of the replacement property is notified of ABC's assignment of rights to QI to buy replacement property. On QI's website, ABC directs QI to reinvest the restricted proceeds from the sale of the relinquished property in the identified like-kind replacement property. The statutory identification and replacement periods are met.

Both the buyer of the relinquished property and the seller of the replacement property are notified of the assignment of ABC's rights regarding the transaction via e-mails. ABC can

identify by model and serial number both the property it gives up as well as the replacement property it acquires.

Transaction is a like-kind exchange. IRS ruled that:

- (1) ABC's transfer of each batch of relinquished properties, and its corresponding receipt of related replacement properties, is a separate and distinct like-kind exchange under Code Sec. 1031;
- (2) QI is treated as a qualified intermediary; and
- (3) ABC won't be in constructive receipt of any of the proceeds from the sale of relinquished property or any money or other property held by QI unless and until such amounts or items are actually received by ABC (i.e., if replacement property isn't acquired during the exchange period and the sale proceeds are transferred to ABC).

 **RIA observation:** In other words, QI may operate as an electronic third-party facilitator to turn ABC's sale of equipment and reinvestment in like-kind equipment into a transaction treated as a tax-deferred Code Sec. 1031 exchange.

References: For deferred exchanges, see FTC 2d/FIN ¶ I-3095; TaxDesk ¶ 224,200; United States Tax Reporter ¶ 10,314.10; TG ¶ 10380.